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INTERNATIONAL COUNTERTRADE

Draft Legal Guide on International Countertrade Transactions

Report of the Secretary-General

Addendum

IV. COUNTERTRADE COMMITMENT

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[Editorial note: The present draft chapter IV incorporates revised draft chapter VII, "Fulfilment of countertrade commitment" as it appeared in A/CN.9/332/Add.8, revised paragraphs 26 and 27 from draft chapter V, "Type, quality and quantity of goods" as it appeared in A/CN.9/332/Add.4, and revised section C of draft chapter III, "Contracting approach", as it appeared in A/CN.9/332/Add.2. The revisions of paragraphs are underlined. The note in square brackets at the beginning of some paragraphs indicates that those paragraphs are new. An asterisk indicates the place where text has been deleted without adding new language.]

A. General remarks

1. [new paragraph] A countertrade commitment, a commitment to conclude a future contract, is an essential feature present in two types of countertrade transactions. The first type is when the parties at the outset of the transaction finalize a contract in one direction (export contract) and then commit themselves to conclude a counter-export contract (see chapter III, paragraphs 13 to 19); the second type is when the parties commit themselves at the outset of the transaction to conclude a series of supply contracts in the two directions (see chapter III, paragraphs 20 and 21). The term countertrade commitment is explained in chapter II, paragraph 25.

2. [new paragraph] The degree to which parties may commit themselves to enter into a future contract may range from a "firm" commitment to enter into a supply contract to a more limited "serious intention" type of commitment (referred to also as "best efforts" or "good faith" commitments). Under a firm countertrade commitment, the parties undertake to conclude a contract in accordance with the terms set out in the countertrade agreement, without retaining a discretionary right to refuse to conclude a contract. Under a serious-intention type of commitment, the undertaking is limited to an obligation to negotiate in good faith, with a party retaining the right to refuse to enter into a contract if none of the contract offers is acceptable to it. Under the latter commitment, any sanctions for failing to comply with the commitment can apply only in the limited cases when the party fails to participate in negotiations or does not negotiate in good faith. The Legal Guide focuses on firm countertrade commitments. It does not deal with serious-intention type of commitments since such commitments do not provide sufficient assurance to the parties that the objectives of the countertrade transaction will be achieved.

B. Extent of countertrade commitment

3. [new paragraph] The extent of a countertrade commitment is frequently expressed in a monetary value. In counter-purchase, buy-back or indirect offset transactions, in which the parties conclude first a supply contract in one direction (export contract) (see chapter III, paragraphs ...), the extent of the countertrade commitment is often expressed as a percentage of the value of the goods delivered under the export contract. In countertrade transactions in which the parties conclude the countertrade agreement prior to concluding an unspecified number of contracts in the two directions (see chapter III, paragraphs 20 and 21), the extent of the purchases to be made in

the two directions is often defined by an absolute monetary amount. Sometimes, however, the countertrade commitment is quantified by reference to a specific quantity of a given type of goods. It should be noted that the extent of the countertrade commitment may be subject to governmental regulations.

4. [new paragraph] In countertrade transactions with successive deliveries (e.g., buy-back transactions), in long-term transactions, or in transactions where the counter-exporter's financing costs are uncertain at the time of the conclusion of the countertrade agreement (e.g., because of a floating-rate credit arrangement), clauses are sometimes found providing for an increase or a decrease of the countertrade commitment depending upon movement in prices of the goods in question or in financing costs. In the case of capital goods, it may be agreed that the commitment will be increased in proportion to expenses for spare parts or technical assistance.

5. [from A/CN.9/332/Add.4, para. 26] When the purchaser has made prior purchases from the supplier of a given type of goods, the provisions in the countertrade agreement regarding quantity may contain a concept often referred to as "additionality". According to this concept, only those purchases that exceed the usual quantities purchased will be considered as fulfilling the countertrade commitment. The parties would normally be able to establish the threshold of additionality by agreeing on the quantity that is to be regarded as the usual or traditional purchase. When the parties do not identify the type of goods in the countertrade agreement, they may include a general stipulation that if the goods ultimately selected are of a type that the purchaser is already buying, only those purchases above existing levels would be counted toward fulfilment of the countertrade commitment.

6. [from A/CN.9/332/Add.4, para. 27] Where the arrangement allows the purchaser to choose from a number of eligible suppliers other than the party to whom the countertrade commitment is owed (e.g., in an indirect offset transaction), the additionality threshold would not be based on previous trade volume between the parties to the countertrade agreement, but on the trade volume with the suppliers selected or on the volume of previous purchases by the committed party in the suppliers' country. In defining the additionality threshold, the parties may, for example, agree on an amount of purchases that is to be considered as the usual or traditional amount of purchases, which would not be counted towards fulfilment of the countertrade commitment. The parties may also stipulate that purchases from specified types of suppliers or from certain specified suppliers, or purchases from those suppliers that do not exceed an agreed amount, are to be regarded as the usual or traditional purchases. In some cases, the parties may wish to apply an additionality threshold only to certain types of goods. The parties may provide in the countertrade agreement that the party committed to purchase can count its purchases toward the fulfilment of the countertrade commitment after it has been established in an agreed manner that purchases agreed to be regarded as usual or traditional have been made.

C. Time period for fulfilment of countertrade commitment

[The present section C incorporates, with underlined modifications, paragraphs 17 to 30 of draft chapter VII, "Fulfilment of countertrade commitment" as it appeared in document A/CN.9/332/Add.8.]

1. Length of fulfilment period

7. The parties should specify in the countertrade agreement the length of time to be allowed for fulfilment of the countertrade commitment (hereinafter referred to as the "fulfilment period"). The countertrade agreement may determine the length of the fulfilment period by stipulating that the fulfilment period is to commence upon a fixed date and to expire on a fixed date.

8. Another method is to make the commencement of the fulfilment period contingent upon an event specified in the countertrade agreement and to set the length of the fulfilment period. Such an approach may be desirable in a variety of circumstances. For example, when the conclusion of the countertrade agreement precedes the entry into force of the export contract, the parties may agree that the fulfilment period will not begin until the export contract has entered into force. When there is uncertainty at the time of the conclusion of the countertrade agreement about the availability of countertrade goods or about the ability of the purchaser to utilize or market them, the parties may agree that the fulfilment period will commence upon the completion of certain preparatory activities (e.g., identification of goods, inspection by purchaser, certification of the technical capability of the factory producing the goods, agreement with a third-party purchaser or completion of joint marketing research). Where the exporter wishes to ensure that performance of the export contract is at an advanced stage or completed before performance of the countertrade commitment commences, the parties may stipulate in the countertrade agreement that commencement of the fulfilment period is to be triggered by an event in the performance of the export contract such as the opening of the letter of credit, delivery of a specified portion of the goods or payment. In a buy-back transaction, an appropriate moment might be the beginning of production of buy-back products by the facility supplied under the export contract. In order to avoid uncertainty as to whether the conditions for commencement of the fulfilment period have been met, it is advisable that the countertrade agreement state those conditions and the related obligations of the parties as precisely as possible.

9. In determining the length of the fulfilment period the parties should consider a number of factors. One factor is the size and type of the transaction being contemplated. For example, where the countertrade commitment is large and involves a series of shipments, more time would normally be needed for fulfilment of the countertrade commitment than if the transaction were relatively small. Where the countertrade agreement defines the countertrade goods in broad terms, it may be that a longer fulfilment period would be needed in order to allow time for identifying suitable countertrade goods. The quality of the countertrade goods may affect the length of the fulfilment period. The better the quality, the more likely it will be that the purchaser will either be able to market or use them in-house, thus allowing a shorter fulfilment period.

10. In some cases, the length of the fulfilment period is set so that it extends beyond the date when payment is due under the export contract. Such an approach would allow the exporter time to fulfil the countertrade commitment after payment under the export contract is due. In such a case it is in the interest of the importer to include in the countertrade agreement effective sanctions for breach of the countertrade commitment.

11. The parties may agree that the fulfilment period for the shipment in one direction is to be of the same length as the fulfilment period for the shipment in the other direction. Such an approach may be appropriate when no particular importance is attached to the order of the shipments in the two directions (e.g., countertrade carried out within the framework of a setoff account (chapter IX, "Payment", paragraphs ____) or an evidence account (paragraphs 68 to 74 below)). Such an approach may also be appropriate in a counter-purchase transaction in which the counter-importer is prepared to begin fulfilling the countertrade commitment without waiting to be paid under the export contract.

12. The fulfilment period should be of a sufficient length to take into account difficulties the supplier may encounter in making the countertrade goods available. If the goods are not made available in time, the purchaser could object to the exercise by the supplier of remedies for non-fulfilment of the countertrade commitment by claiming that non-fulfilment was due to unavailability of the goods. If the purchaser is entitled to select the goods from a list of eligible countertrade goods, the length of time needed to make available each of the different goods listed should be taken into account calculating the length of the fulfilment period.

2. Extension of fulfilment period

13. The parties may require more time to fulfil the countertrade commitment than provided by the countertrade agreement. For example, a purchaser may encounter unanticipated difficulties in utilizing or reselling the goods to be purchased. A supplier may have difficulties in making agreed upon goods available on schedule.

14. The law applicable to the countertrade agreement may provide for an extension of the time allowed for the performance of a party's contractual obligations in the event that the possibility of performance is affected by circumstances beyond the control of that party. The parties may wish to include in the countertrade agreement clauses addressing such situations (see chapter XIII, paragraphs ___, for a discussion of exemption * clauses).

15. The countertrade agreement may provide that the parties will negotiate an extension if the party seeking an extension has made reasonable efforts to fulfil the commitment. Alternatively, the parties might agree that, if the party made reasonable efforts to fulfil the commitment, that party would be entitled to an appropriate extension of the fulfilment period. It may be left to the parties to agree on the new fulfilment period. The countertrade agreement might indicate how the purchaser could demonstrate reasonable efforts. For example, in an indirect offset, it may be provided that the purchaser would have to show that it had made reasonable offers to potential suppliers to purchase goods, or that it had contacted a reasonable number of potential suppliers in search of suitable countertrade goods, or that potential suppliers had indicated that they would be willing to enter into

supply contracts some time after the expiry of the fulfilment period. Evidence of such reasonable, but unsuccessful, efforts are sometimes in practice referred to as "negative files". The countertrade agreement may also provide that a supplier who was unable to make goods available due to circumstances specified in the countertrade agreement would be entitled to an extension. Such circumstances may include, for example, lateness of the purchaser's order or changes in the purchaser's specifications. The parties may agree that a party could request an extension of the fulfilment period only if that party had fulfilled a portion of the countertrade commitment.

16. If the fulfilment of the countertrade commitment is supported by a guarantee, it is advisable that the parties provide that the period of the guarantee should be extended to cover an extension of the fulfilment period (see chapter XII, "Security for performance", paragraphs ____).

3. Subperiods within fulfilment period

17. Where fulfilment of the countertrade commitment involves many shipments over a long period of time, the parties may wish to divide the fulfilment period into subperiods. For example, a five-year fulfilment period could be divided into five annual subperiods, with a specified portion of the total commitment to be fulfilled during each subperiod. Such an approach assists the parties in planning delivery and marketing of the countertrade goods, and helps to ensure that fulfilment does not fall so far behind that the parties would be unable at the latter stages of the fulfilment period to fulfil the outstanding countertrade commitment.

18. The countertrade agreement may allow flexibility in dealing with shortfalls in the fulfilment of the commitment assigned to individual subperiods by permitting the carry-over of all or a portion of a shortfall to the next subperiod. In such a case, the purchaser would have, in the following subperiod, to fulfil the portion of the commitment allocated to that subperiod, as well as to fulfil the portion of the commitment carried over from the preceding period. The portion not carried over would be subject to sanctions for failure to fulfil the countertrade commitment (see chapters XI, "Liquidated damages and penalties", and XII, "Security for performance"). Such flexibility would allow the purchaser to adjust the quantity to be purchased in a given subperiod in response to circumstances such as short term market fluctuations. However, a high degree of flexibility might adversely affect the interests of the supplier if the proceeds of sales in each subperiod are to be used for payments under the supply contract in the other direction.

19. To address the possibility that the fulfilment achieved in a given subperiod exceeds the required level, the parties may agree that some or all of the extra purchases would be credited to the commitment due in the following subperiod. Alternatively, the parties may agree that the excess fulfilment in one subperiod would not affect the level of the commitment due in the following subperiod.

20. The parties may wish to set deadlines within the fulfilment period for completion of different actions that precede fulfilment of the countertrade commitment. For example, the parties could stipulate deadlines for providing samples of countertrade goods, selecting goods from a list of possible countertrade goods, placing orders, shipping goods or opening letters of credit.

D. Defining eligible supply contracts

[The present section D incorporates, with the addition of two new paragraphs, paragraphs 2 to 9 of draft chapter VII, "Fulfilment of countertrade commitment" as it appeared in A/CN.9/332/Add.8.]

21. The parties normally define the supply contracts that will be counted towards fulfilment of the countertrade commitment ("eligible supply contracts") by indicating in the countertrade agreement the type of goods to be purchased under those future supply contracts. In some cases, the parties include in the countertrade agreement additional criteria relating to the geographical origin of the goods, the identity of the supplier, or the identity of the purchaser. When the parties are not in a position to indicate the type of goods in the countertrade agreement, some of these criteria may be included for the purpose of defining eligible supply contracts.

1. By type of goods

22. When the parties define the contracts eligible to be counted towards fulfilment by indicating the type of goods to be purchased, it is advisable that they do so with as much precision as possible. Precision is particularly advisable when the goods to be purchased exist in different varieties. (For a discussion of clauses in the countertrade agreement concerning the type of goods, see chapter V, "Type, quality and quantity of goods", paragraphs 3 to 23.)

23. Sometimes the parties provide in the countertrade agreement that, in addition to the purchase of the countertrade goods, other related items are to be counted towards fulfilment of the countertrade commitment. Such ancillary items may be, for example, purchase of samples and prototypes in the course of selecting the countertrade goods, local contracting of labor, local purchase of goods and services essential for carrying out a supply contract, unbilled activities by the purchaser in the supplier's country (e.g., recruitment of personnel, training programs, secondment of staff and other forms of technical assistance), purchase from the supplier of transportation services, or performance by the purchaser of after-sales service on the countertrade goods. The countertrade agreement may provide that only a limited portion of the countertrade commitment may be fulfilled through such items.

24. When the purchaser has made prior purchases from the supplier, the countertrade agreement may provide that supply contracts must meet an "additionality" requirement in order to be counted toward fulfilment (see above, paragraphs 5 and 6).

25. [new paragraph] It should be noted that stipulations on eligibility of supply contracts based on the geographical origin of goods might conflict with mandatory rules of competition law and rules adopted pursuant to the General Agreement on Tariffs and Trade (GATT).

2. By geographical origin

26. Eligibility of supply contracts may be defined by a stipulation that countertrade goods must be produced in a particular geographical area. Stipulations of this type are sometimes found in indirect offset transactions where the importer wishes to channel the counter-purchases to a particular

region. Furthermore, the countertrade agreement may stipulate a required minimum level of local content. Such stipulations may provide that particular components of the goods must be locally produced or that the value of local components must constitute a certain percentage of the total value. Local content requirements are sometimes found in governmental regulations.

27. [new paragraph] As in the case referred to above in paragraph 25, stipulations requiring a party to purchase goods from identified suppliers might conflict with mandatory rules of competition law and provisions adopted pursuant to the General Agreement on Tariffs and Trade (GATT).

3. By identity of supplier

28. The parties may agree that the exporter is to fulfil the countertrade commitment by purchasing goods from persons other than the importer. This is typically the case in indirect offset (see chapter II, paragraph 17). In such cases, it is advisable that eligible supply contracts be defined by identifying the suppliers from whom the goods are to be purchased. The countertrade agreement may list eligible suppliers or may stipulate criteria to be observed by the purchaser in selecting a supplier. It may be provided, for example, that a selected supplier must be from a particular economic sector, be of a certain size, have a particular production programme, be located in a particular region, or be locally owned. Where several eligible suppliers are identified, the purchaser may be left free to distribute purchases among various suppliers or a particular structure of purchases from the identified suppliers may be stipulated. The identification of eligible suppliers does not necessarily mean that those suppliers have made a commitment to make countertrade goods available. In some cases the importer may provide an assurance that the eligible suppliers are prepared to negotiate the conclusion of a supply contract or the importer may promise to assist the purchaser in identifying a supplier who is willing to conclude a supply contract. (For a discussion of the participation of third persons as suppliers, see chapter VIII, paragraph .) The countertrade agreement may indicate the effect on the countertrade commitment if none of the eligible suppliers are prepared to conclude a supply contract.

4. By identity of purchaser

29. A restrictive element sometimes found in the definition of eligible supply contracts concerns the identity of the purchaser. For example, the countertrade agreement may provide that only purchases made by the party committed to purchase goods or by specified third persons (e.g., third persons from a particular country or geographical region) are to be counted toward fulfilment. For a discussion of restrictions on the participation of third persons as purchasers, see chapter VIII, paragraph .

5. Non-conforming purchases

30. The parties may agree that under certain circumstances purchases that do not conform to the eligibility requirements in the countertrade agreement would nevertheless be counted toward fulfilment of the countertrade commitment. For example, non-conforming purchases could be counted if the good faith efforts of the purchaser to locate suitable goods from the eligible suppliers or in the geographical regions or economic sectors identified in the countertrade agreement were unsuccessful. A provision of that type could call

upon the purchaser to provide evidence of efforts to make purchases of the type required by the countertrade agreement (for a discussion of the analogous case of a party requesting an extension of the fulfilment period, see above, paragraphs 13 to 16). It could be agreed that the specific prior consent of the party to whom the commitment is owed would be necessary for the purchases not meeting the eligibility requirements to be counted toward fulfilment. In order to foster efforts to comply with origin requirements, the countertrade agreement could limit the availability of an exception to the later stages of the fulfilment period. Furthermore, the parties may agree that purchases counted toward fulfilment that fall outside the eligibility provisions are to be counted at less than the full value of the purchases (see paragraphs 32 and 33 below).

E. Rate of fulfilment credit [change of title]

[The present section E incorporates, with underlined modifications, paragraphs 13 to 16 of draft chapter VII, "Fulfilment of countertrade commitment" as it appeared in A/CN.9/332/Add.8.]

31. In many countertrade transactions, the full purchase price of a supply contract is deducted from the outstanding countertrade commitment (the amount deducted from the outstanding countertrade commitment is hereinafter referred to as "fulfilment credit"). Sometimes the parties agree that the fulfilment credit granted for a supply contract is to be an amount different from the purchase price. One reason for such an approach may be that the parties wish to give fulfilment credit for certain outlays not included in the cost of the goods themselves (e.g., transportation and insurance) or to exclude from the fulfilment credit certain costs included in the purchase price. The supplier may agree to the crediting of such cost elements if, for example, they involve the purchase in the supplier's country of services related to the performance of the supply contract. The rate of fulfilment credit might also be prescribed by mandatory provisions of law (chapter XIV, "Choice of law", paragraphs).

32. The countertrade agreement may provide that purchases are to be credited toward fulfilment of the countertrade commitment at different rates depending upon the type of goods purchased. For example, fulfilment credit could be granted at the rate of 50 percent of the purchase value for one type of goods and 150 percent for another, or that investments or technology transfer will be credited at more than the capital contribution of the investment or the monetary value of the technology transfer (e.g., 150 percent). Such a variable rate of fulfilment credit may be used in particular in indirect offset transactions, in which the exporter concludes contracts with third parties, and the importer wishes to promote the purchase of certain types of goods. * In direct offset, as well as in buy-back, the countertrade agreement may provide that a certain amount of fulfilment credit will be granted for export sales, other than those to the counter-importer, generated by the production facility supplied by the exporter. Credit may also be granted for a percentage of the value of sales to buyers in the counter-exporter's country. A variable rate of fulfilment credit might also be used in transactions in which the supply contracts are to be entered into between the parties to the countertrade agreement, in particular if the purchaser has a choice between several types of goods; in such a case the variable rate may serve as a stimulus to purchase a certain type of goods.

33. The countertrade agreement may also provide for different rates of fulfilment credit depending upon the identity of the supplier, the geographical origin of the goods or the identity of the purchaser. The rationale behind such a provision is to steer the activities of the purchaser towards particular suppliers or regions, or to introduce the goods in certain markets.

34. The rate of fulfilment credit may also be made to vary according to the point of time when a purchase is made. Under a scheme of this type, the purchaser could fulfil the countertrade commitment by the purchase of a smaller quantity of goods if a supply contract was concluded at an early stage of the period for the fulfilment of the countertrade commitment. This approach is designed to give the purchaser an incentive for fulfilling the commitment earlier rather than later in the fulfilment period. In such a case it is particularly important that the countertrade agreement specify the point when fulfilment credit is to be given (e.g., when an order is placed or when payment is made).

F. Stage when commitment fulfilled

[The present section F incorporates, with underlined modifications, paragraphs 10 to 12 of draft chapter VII, "Fulfilment of countertrade commitment" as it appeared in A/CN.9/332/Add.8.]

35. It is advisable that the countertrade agreement indicate the specific action that must be taken in order for the countertrade commitment to be fulfilled. The parties may choose between two basic approaches. Under one approach, the countertrade commitment is deemed to be fulfilled once a supply contract is concluded. In such cases, a breach of an obligation under the supply contract would be subject to remedies available under the supply contract. The parties may agree that, if the supply contract is not performed due to a reason imputable to one party, the amount of the unperformed contract could, at the option of the other party, be reinstated in the countertrade commitment.

36. Under the second approach, the commitment is deemed to be fulfilled at an agreed stage in the performance of the supply contract. For example, it may be agreed that the commitment of the purchaser is fulfilled when the letter of credit is opened or when the funds have been transferred to the supplier and that the corresponding commitment of the supplier is fulfilled when the goods are delivered or placed at the disposal of the purchaser in the agreed manner. In such cases, in the event of a breach of the supply contract, the aggrieved party might be able to invoke remedies not only for breach of the supply contract, but also for breach of the countertrade agreement if the countertrade commitment remained unfulfilled. A disadvantage of this second approach is that it is more complicated and uncertain than the first approach, under which fulfilment is deemed achieved simply upon the conclusion of a supply contract. The second approach might result in uncertainty when exempting impediments affect the ability of a party to take the steps necessary in the performance of a supply contract to achieve fulfilment of the countertrade commitment. In order to avoid this uncertainty, additional provisions would be required in the countertrade agreement on the effect of such impediments.

37. The parties may wish to address the effect on the countertrade commitment of a failure to conclude or perform a supply contract. It may be agreed, for example, that when the reason for such a failure is imputable to one of the parties, the outstanding countertrade commitment of the other party may, at the option of that other party, be deemed fulfilled in the amount of the unaccepted contract offer or unperformed contract (see chapter XIII, "Failure to complete countertrade transaction", paragraph).

G. Defining terms of future supply contracts

[The present section G is a restructured section C, paragraphs 37 to 61, of draft chapter III, "Contracting approach" as it appeared in A/CN.9/332/Add.2. Paragraps 39 to 42 of the earlier section C, A/CN.9/332/Add.2, entitled "Negotiation procedures", have been included at the end of the present subsection 6.]

1. Terms of future supply contracts

38. [paragraph 43 in A/CN.9/332/Add.2] Commitments to enter into supply contracts often do not stipulate in a definite manner all the terms of the contracts to be concluded. Sometimes the parties have not decided yet on the type of goods that will be the subject of the future supply contracts or what the terms of delivery will be. Even if the parties are able to set out in the countertrade agreement terms of the future supply contract, they sometimes forego doing so because they expect each party to live up to the commitment to conclude a future contract, though the terms of that contract may not be defined in great detail in the countertrade agreement.

39. [new paragraph] A lack of definiteness of the countertrade commitment may result in delays or uncertainties in negotiating a supply contract in view of the potentially broad scope of the negotiations. It is therefore advisable that the parties, to the extent feasible, include in the countertrade agreement the terms of the future contract or provide for means for subsequent determination of those terms (see paragraphs 44 to 56 below). In addition, the parties may wish to address in the countertrade agreement procedures to be followed in their negotiations (see paragraphs 57 to 60 below). This will facilitate negotiations, increase the likelihood that a supply contract will be concluded and increase the possibility that the party interested in the conclusion of the contract would be able to hold the other party responsible for refusing to conclude the contract. If, for example, the countertrade agreement specifies the goods that a party is committed to purchase, or at least contains a list of goods as a basis of negotiations, the counter-exporter may be able to show that the refusal of the counter-importer to purchase any goods constitutes a breach of the countertrade commmitment. If the goods are specified, it is also advisable to provide a mechanism for determining the price; this is particularly important when the countertrade goods are not of a standard type and it may be open to disagreement what is a fair market price.

40. [paragraph 46 in A/CN.9/332/Add.2] As the countertrade agreement becomes more definite in specifying the terms essential for the existence of an enforceable contract, the agreement approaches the point at which the parties have settled all the terms of the supply contract and postponed only the act of concluding the contract. When the countertrade agreement embodies the essential terms of the future contract for the purchase of goods, in some

legal systems the possibility exists that such a countertrade agreement could be relied upon as an enforceable sales contract. In order to avoid disagreements, it is advisable that the parties, when concluding a countertrade agreement that contains the essential terms of the contract to be concluded, stipulate clearly whether a separate contract is to be executed pursuant to the countertrade agreement.

41. [paragraph 47 in A/CN.9/332/Add.2] Many legal systems contain rules to which the parties may resort in order to provide definiteness to a contract clause. For example, numerous legal systems provide a solution when the parties have not settled the price of the goods; the solution may be, for instance, that the price should be the one "generally charged at the time of the conclusion of the contract for such goods sold under comparable circumstances in the trade concerned" (article 55 of the United Nations Convention on Contracts for the International Sale of Goods). Another example may be the rule on the quality of the goods to be delivered under the contract when the contract has not settled that issue; the rule in article 35(2)(a) of the above-mentioned Convention is that the goods should be "fit for the purposes for which goods of the same description would ordinarily be used". In some legal systems the parties may, within certain limits, resort to a court for the purpose of determining such a contract element. In other legal systems, however, the courts are not competent to intervene in this manner in a contractual relationship.

42. [paragraph 48 in A/CN.9/332/Add.2] Although such means for contract supplementation exist in many legal systems, they normally do not provide a solution in all cases of indefiniteness. The contract elements left indefinite in the countertrade agreement may not lend themselves to being made definite by reference to the applicable law. For example, if the parties have not agreed on the type of goods to be counter-exported, it would probably be impossible to determine the type on the basis of the applicable law. Where the type of goods has been settled, the criteria provided in the applicable law concerning the price of the goods may not lead to a clear solution. Furthermore, such contract supplementation is subject to uncertainty arising out of divergencies among legal systems as to the techniques of supplementation, the role of the courts or arbitral tribunals in determining the missing term, the role of the parties, or as to the judicial control over the result of the supplementation. * As a result, the parties may wish to consider the contractual means discussed below for providing definiteness to a contract term left open in the countertrade agreement.

43. [paragraph 49 in A/CN.9/332/Add.2] The terms that are often left indefinite in the countertrade agreement and with respect to which contractual means for completing indefinite terms may be particularly useful are the type, quality, price and quantity of the countertrade goods. The contractual means that the parties may consider for completing any one or more of those terms are discussed in a general manner in subsections (a) through (c) below. In other parts of the Legal Guide, these contractual means will be referred to in specific contexts.

(a) Standards or guidelines

44. [paragraph 50 in A/CN.9/332/Add.2] The parties may wish to provide standards or guidelines to be used in determining particular contract terms. The use of a standard would allow the parties to determine a contract term by

computation or by some other objective method not dependent upon the discretion of the parties. Examples of such standards include a formula, tariff, quotation, rate, index, statistic, or some other criterion not influenced by the will of either party. For example, the price of the countertrade goods may be determined by reference to the price at which goods of the same type are sold in a particular market or exchange, or the quality of the countertrade goods may be defined by reference to a particular national or international quality standard. Many legal systems recognize as valid a provision that the price or other contract term should be determined by reference to a standard.

45. [paragraphs 50 and 45 in A/CN.9/332/Add.2] Guidelines, on the other hand, set parameters within which a contract term is to be determined and involve a degree of latitude in arriving at a contract term. For example, the countertrade agreement may set a range within which the parties are to negotiate the price or it may be agreed that the price must be "reasonable" (such price clauses are further discussed in chapter VII, "Pricing of goods", paragraphs). [The following underlined text has been taken from from para. 45 of A/CN.9/332/Add.2:] Sometimes the parties are not in a position to be more definite about the terms of the anticipated supply contract than to provide that the contract terms should be fair or in accordance with the prevailing market conditions. Such provisions may be helpful when countertrade goods of a standard quality are agreed upon, thereby enabling a fair price to be ascertained. If, however, the type of countertrade goods is not settled or if the countertrade goods are products that do not have a standard price, such a "fair terms" commitment may not substantially enhance the position of the party interested in the conclusion of the contract. In such cases opinions may differ as to what contract terms are fair, thereby protracting the negotiations and making uncertain the success of a claim against the party refusing to conclude the contract. If the type of goods has not been determined, the parties may agree on a list of goods on which the negotiations should focus or to which it should be limited (such lists are discussed in chapter V, "Type, quality and quantity of goods"). As to other terms of the future contract, such as delivery, the parties may agree that the supply contract should be negotiated on the basis of prevailing market conditions. Where reference is made to market conditions, it is advisable that the parties refer to a specific market.

46. [paragraph 52 in A/CN.9/332/Add.2] Because of the discretion left to the parties, the inclusion of a guideline in the countertrade agreement for a particular term in the future contract does not ensure the finalization of that term. Nevertheless, a narrow range within which agreement should have been achieved, or clear guidelines limiting the latitude available to the negotiators, will not only make it more likely that a contract will be concluded but will also make it easier to show that a party refusing a given contract offer is in breach of the countertrade commitment.

(b) Determination of contract term by third person

47. [paragraph 53 in A/CN.9/332/Add.2] Sometimes the parties agree that a particular contract term will be determined by a third person. While such an approach provides a high degree of certainty that the term will be made definite, its infrequent use may be attributable to a reluctance by parties to relinquish their control over a contract term. When such a method is used, it is usually to determine the price of goods (see chapter VII, paragraphs and

___). The parties might be willing to agree on such a method of determining a contract term if clear, and preferably narrow, guidelines are established within which the third person is to decide or if the third-person intervention is the last resort after other agreed mechanisms (e.g., negotiation, application of an agreed standard) have failed. If the parties do not wish to entrust the decision on a contract term to a third person, but still want the benefit of the opinion of a third person, it may be agreed that the determination by the third person will only be a recommendation.

48. [paragraph 54 in A/CN.9/332/Add.2] A number of legal systems recognize the right of the parties to entrust a third person with determining a contract term. In particular, reference by the parties to a third person for the determination of the price is a question frequently addressed in legal systems. There are, however, variations among the systems. For example, while some legal systems recognize that an arbitral tribunal or even a court may be entrusted with the determination of a contract term, others permit such a determination only if it is not performed as part of arbitral or judicial proceedings. Legal systems also differ as to the consequences of a failure by the parties to agree on the third person or of a failure by the third person to act. Under some legal systems, the parties would have no recourse to a procedure for designating or replacing the person, and would have to accept the consequences of the contract term being left undetermined. In other systems, if the third person was to determine the price, the case may be treated as if the parties had agreed on a reasonable price. There are also differing approaches to the availability and extent of judicial review of a decision by a third person.

49. [paragraph 55 in A/CN.9/332/Add.2] The issues that the parties may wish to address in a stipulation empowering a third person to determine a contract term are discussed in the following paragraphs.

50. [paragraph 56 in A/CN.9/332/Add.2] Person to request determination of term. The parties may wish to address the question whether, at the time when the parties fail to agree on the term, either party would be entitled to request the third person to determine the term or whether the third person may act only upon the request of both parties.

51. [paragraph 57 in A/CN.9/332/Add.2] The identity of the third person or the appointment procedure. The parties may wish to name in the countertrade agreement the person who is to determine the contract term. In this case, the parties may also wish to provide an appointment procedure to be used in the event that the named person fails to act or is unable to act. If the parties do not wish to name the person who is to determine the contract term, it may be advisable for the parties to agree that they will appoint the third person at such time as they are unable themselves to reach agreement on the contract term. In such a case the parties may wish to agree on an appointment procedure, which is to become operative if the parties cannot reach agreement on the appointment of the third person.

52. [paragraph 58 in A/CN.9/332/Add.2] Guidelines or standards to be observed by third person. The parties are advised to delimit the mandate of the third person by providing guidelines or standards to be observed in determining the contract term. Such guidelines and standards are discussed generally above, paragraphs 50 to 52, and, as to price, in chapter VII, "Pricing of goods", paragraphs to .

53. [paragraph 59 in A/CN.9/332/Add.2] Nature of decision of third person. The parties may agree that the decision by the third person would be binding as a contractual stipulation of the parties. Another approach may be to provide that the determination of the third person would be treated as a recommendation to be considered by the parties in good faith.

54. [paragraph 60 in A/CN.9/332/Add.2] Procedure for challenging decision by the third person. In some situations, for example, where the binding determination by the third person involves a question of particular economic significance, the parties might wish to provide an opportunity for the decision to be challenged by resort to another person, a panel of persons, or an institution. As to the nature of the decision on the challenge, it may be provided that the decision would bind the parties or only be a recommendation. The parties may wish to stipulate the mandate that would be given to the person deciding on the challenge (i.e., to uphold or reject the challenge, or to modify the challenged decision). The parties may wish to indicate how, in the event the challenged decision is set aside, the decision on the contract term is to be made (e.g., by the parties themselves or by the same or a different third person).

(c) Determination of contract term by contract party

55. [paragraph 61 in A/CN.9/332/Add.2] Sometimes the countertrade agreement leaves the determination of a contract term to one of the parties to the countertrade agreement. Utmost caution is advisable in agreeing on such a solution, which leaves the determination of the contract term to a person who has an interest in the outcome of the determination.

56. [paragraph 61 in A/CN.9/332/Add.2] The parties should be aware that a clause empowering a contract party to determine a contract term is in many legal systems not enforceable. Where such a clause is recognized, it is subject to strict conditions. If the subject of the determination is the price, a number of systems would recognize such a right given to a party if its exercise is limited by such standards as reasonableness, good faith or fairness. Some of these systems would construe an agreement not expressly referring to such a standard as implicitly referring to it. Other legal systems require the freedom to determine the price to be limited by a more definite standard such as objectively ascertainable market prices, price averages or absolute limits stipulated by the parties. Analogous restrictions apply to the determination of terms such as the quantity of goods to be delivered under a contract or the time of contract performance.

2. Negotiation procedures

57. [paragraph 39 in A/CN.9/332/Add.2] Countertrade agreements may set forth with varying degrees of procedural detail the manner in which negotiations are to be carried out. Specifying the negotiation procedures increases the probability that the negotiations will lead to a successful outcome. This would be particularly true where the nature of the negotiations is likely to be complicated, either because of the subject matter of the eventual contracts or because of the number of persons who might be involved in those negotiations.

58. [new paragraph] Care should be taken to make negotiating procedures a part of a firm undertaking to conclude a supply contract. If the undertaking

is limited to a mere obligation to negotiate, the parties, as noted above in paragraph 2, will have little assurance that the objectives of the transaction will be achieved. Even if negotiating procedures are combined with a firm countertrade commitment, such procedures alone do not ensure that negotiations will be successful. The most effective way to increase the likelihood of succeeding in the negotiations would be either to stipulate in the countertrade agreement the terms of the future contract or, if this is not possible, to agree on means for providing definiteness to the countertrade commitment. Such means are discussed above, in particular in paragraphs 44 to 56.

59. [paragraph 40 in A/CN.9/332/Add.2] At a minimum, the countertrade agreement might provide that a party would be obligated to respond to contract proposals by the other party. More specific procedures would address issues such as: the party who is to submit a contract offer; questions to be covered by a contract offer; time periods for submitting it; the form, means or frequency of communication; the time period for reply; the time within which an agreement must be reached, and beyond which negotiations will be deemed to have failed. Furthermore, the parties may provide that in certain circumstances a party would be relieved of the duty to negotiate (e.g., when that party has made an offer meeting the agreed conditions and it has not been accepted, or, if the other party was to make the offer, when no such offer has been made).

60. [paragraph 41 in A/CN.9/332/Add.2] The stipulation of negotiation procedures such as those mentioned in the previous paragraph may * increase the possibility that a party who has not negotiated in good faith could be held responsible for the failure to conclude a contract. Such procedures could enable an aggrieved party to demonstrate, for example, that the other party refused to negotiate, imposed conditions to negotiate that the party could not properly impose, used unfair dilatory tactics, reopened discussion on issues already agreed upon, negotiated with other parties when it was improper to do so, or prematurely broke off negotiations.

H. Monitoring and recording fulfilment of countertrade commitment

[The present section H incorporates, with some underlined modifications, paragraphs 31 to 44 of draft chapter VII, "Fulfilment of countertrade commitment" as it appeared in A/CN.9/332/Add.8.]

61. The parties may wish to consider establishing procedures for monitoring and recording the progress made in fulfilment of the countertrade commitment. Such arrangements may be particularly useful in long term countertrade transactions with multiple shipments in one or both directions.

1. Exchange of information

62. The parties may wish to establish procedures for exchange of information on progress in the fulfilment of the countertrade commitment. Such procedures may be useful, in particular, in "indirect offset" transactions (chapter II, paragraph 17), since the countertrade commitment is owed to a person who does not act as the supplier of the countertrade goods and the potential suppliers are, therefore, not parties to the countertrade

agreement. A system of exchange of information may also be useful when the parties are engaged in a large volume of mutual trade, especially when only a part of that trade stems from the countertrade agreement.

63. The parties may include in the countertrade agreement guidelines concerning the contents, frequency and timing of the information to be exchanged. The required information could cover, for example, contracts that have been concluded and are eligible to be counted towards fulfilment (especially when concluded with a third person), shipments that have been made, payments effected in accordance with agreed upon procedures and purchases planned for an upcoming subperiod of the fulfilment period. Furthermore, the parties to the countertrade agreement sometimes find it useful to meet periodically to assess the progress that is being made towards fulfilment. Such meetings could be used to review the status of concluded contracts and those under negotiation and to consider possible modifications of the countertrade agreement. The countertrade agreement could address questions such as the frequency and location of meetings and the representation of the two sides.

64. In particularly complex transactions that require ongoing monitoring and coordination, the parties may wish to establish in the countertrade agreement a joint coordination committee. It is advisable that the parties address issues such as the frequency and location of meetings, representation of the two sides, the manner in which the results of the meetings will be reported and the mandate of the committee. The mandate of such a committee would typically be to assess progress in the implementation of the transaction, analyse difficulties and consider possible solutions, establish working groups for specific problems, and consider proposals to amend the countertrade agreement.

2. Confirmation of fulfilment of countertrade commitment

65. The parties may agree that the purchaser has a right to obtain from the party to whom the countertrade commitment is owed a written confirmation of the fulfilment of the countertrade commitment. Such a confirmation may take the form of a statement from the supplier (sometimes referred to as a "letter of release"). The parties may agree that the letter of release is a condition for payment under the supply contract concluded in fulfilment of the countertrade commitment (e.g., the letter of credit terms may specify that the letter of release is to be among the documents presented to the bank in order to obtain payment). Fulfilment of the countertrade commitment may also be evidenced by a clause in the supply contract stating that the contract is concluded in fulfilment of the countertrade commitment.

66. Written confirmation of fulfilment is intended to avoid disagreements, which may occur after a particular supply contract has been performed, as to whether the contract counts towards fulfilment of the countertrade commitment. Written confirmation may also be helpful to a party who wishes to demonstrate (e.g., in negotiating other countertrade agreements) a record of fulfilling countertrade commitments.

67. Where written confirmations are envisaged in a multiparty transaction (see chapter VIII, "Participation of third parties", paragraphs to), it is advisable that the countertrade agreement indicate whether the fulfilment

of the commitment is to be confirmed by the supplier of the goods or by the party to whom the commitment is owed. Absent such an indication, a disagreement may arise between the purchaser and the party to whom the commitment is owed as to the significance of a statement by a third-party supplier that a supply contract fulfils the countertrade commitment, or of a clause in a supply contract with a third-party supplier to that effect.

3. Evidence accounts

68. The parties may agree that the supply contracts in the two directions are to be recorded in a ledger kept by themselves, by a bank or by a controlling authority. Such a ledger is referred to herein as an "evidence account", a term frequently used in practice. Other terms used in practice include "record account" and "trade account". An evidence account is not a payment mechanism. Rather, it is used only for recording the conclusion, performance and value of supply contracts, with financing and payment being arranged independently. With an evidence account, the parties undertake a countertrade commitment of a given value and then conclude supply contracts in the two directions without having to negotiate a countertrade commitment for each individual supply contract. Evidence accounts may accommodate multiple parties on one or both sides. An evidence account may be particularly useful in a long-term countertrade transaction to monitor the cumulative value of the purchases in the two directions and thereby to assist the parties in dealing with imbalances that may develop.

69. The use of an evidence account may be subject to governmental regulations. Such regulations may determine the manner in which an evidence account is to operate and require administration of the account by a controlling authority such as the central bank or foreign trade bank. An evidence account administered by a controlling authority may provide the purchaser access to a wider variety of countertrade goods and trading partners than might be available without an evidence account administered by the controlling authority. Government regulations may also require authorization of evidence accounts. It may be provided that such authorization would be given only for countertrade transactions exceeding a minimum turnover and to parties with an established presence in a given country. In some cases, an evidence account is authorized with the restriction that purchases by third parties will not be counted towards fulfilment of the countertrade commitment; such a restriction may be imposed when the motive for permitting an evidence account is to establish a long term trading relationship with a particular party. The countertrade goods may be limited to those agreed upon by the parties or those that the controlling authority has an interest in promoting.

70. When the parties are free to establish an evidence account, they may decide to administer the account themselves or to engage a bank or banks to do so. A variety of structures are possible depending on whether the account is administered by one or both of the parties or by one or two banks engaged by the parties. For example, parallel accounts could be established by a party or a bank on each side of the transaction in which supplies are credited and purchases are debited. Each parallel account could in turn consist of two ledgers, one listing contracts concluded in each direction and the other recording payments. If banks are to administer the evidence account, the parties may wish to use the banks that handle payment for the supply contracts.

71. The countertrade agreement should specify the documentation required for triggering entries in the evidence account (e.g., copies of contracts, evidence of letters of credit, or shipping documents). Such documentary requirements should be in line with the provisions in the countertrade agreement concerning the stage when the countertrade commitment is deemed fulfilled (see above, paragraphs 35 to 37). In order to minimize administrative burden, the parties may wish to align to the degree possible the documentary requirements for the evidence account with those of any governmental authority monitoring the countertrade transaction.

72. It is advisable that the parties address in the countertrade agreement deviations from the agreed upon ratio between the values of the shipments to be made in the two directions. It may be agreed that, while the agreed upon ratio must be achieved upon the conclusion of the fulfilment period or at specified points in the fulfilment period, the values of the shipments may deviate from the agreed ratio during the fulfilment period or between the specified points in the fulfilment period. The parties may further agree that deviations during the fulfilment period must remain within a specified range. For example, during the fulfilment period the value of the shipments in one direction should be not less than 60 and not more than 120 per cent of the value of the shipments in the other direction. It may be agreed that, if a party fails to conclude the supply contracts necessary to achieve the agreed upon ratio, the other party is entitled to suspend conclusion of contracts, or to suspend shipment of goods, in the other direction until the ratio is achieved (see also chapter XIII, "Failure to complete countertrade transaction", paragraph). A failure to achieve the agreed ratio may also be made subject to sanctions (see chapters XI, "Liquidated damages and penalties", and XII, "Security for performance"). It is advisable to define in the countertrade agreement small deviations from the ratio that would be tolerated.

73. In order to minimize errors or discrepancies in the evidence account, it is advisable for the parties to agree to verify at fixed points of time the information entered in the account.

74. Where two banks are involved in administering the evidence account, the technical details of the account may be the subject of an interbank agreement. The countertrade parties have an interest in the contents of the interbank agreement, though they are not normally parties to it. It is therefore advisable that the parties consult with the banks to ensure that the evidence account established by the banks is acceptable to the parties.